SCS Agency
Franchise Tax Board

ANALYSIS OF ORIGINAL BILL

Author:	McPherson	Analyst:	Paul Brainin	Bill Number:	SB 83
Related Bills:	See Legislative History	Telephone:	845-3380	Introduced Date:	12/16/96
		Attorney:	Doug Bramhall	Sponsor:	

SUBJECT: Low-income tax credit/Order of credits allowed against net tax technical

SUMMARY

This bill would provide a nonrefundable, low-income tax credit for individual, resident taxpayers equal to an amount resulting from multiplying the taxpayer's net tax by a percentage, determined by the taxpayer's state adjusted gross income (AGI).

EFFECTIVE DATE

As a tax levy, this bill would become effective upon enactment and apply to taxable years beginning on or after January 1, 1997, and before January 1, 2001.

LEGISLATIVE HISTORY

AB 53 (Stats. 1987, Ch. 1138), AB 2055 (1996).

PROGRAM HISTORY/BACKGROUND

Prior to its sunset in 1992, California law provided a nonrefundable low-income tax credit of an amount ranging from 20% to 100% of the "computational tax," as defined, based on the taxpayer's AGI. The AGI amounts were indexed annually by the department. The "computational tax" was defined as the regular tax less all nonrefundable tax credits. This low-income tax credit could only be taken after all other allowable credits, except refundable credits, had been taken.

SPECIFIC FINDINGS

Existing state law provides various personal credits to taxpayers that may reduce (but not below zero) their amount of income tax.

Existing federal law allows eligible individuals a refundable earned income credit (EIC). The credit percentage and amount vary based on the taxpayer's earned income and whether the taxpayer has qualifying children. The credit also is phased-out where earned income (EI) or AGI exceeds certain dollar thresholds.

DEPARTMENTS THAT MAY BE AFFECTED:

____ STATE MANDATE ____ GOVERNOR'S APPOINTMENT

Department Director Position:	Agency Secretary Position:	GOVERNOR'S OFFICE USE
____ S ____ O ____ SA ____ OUA __X_ N ____ NP ____ NA ____ NAR ________ PENDING	____ S ____ O ____ SA ____ OUA ____ N ____ NP ____ NA ____ NAR DEFER TO ____________	Position Approved ____ Position Disapproved ____ Position Noted ____
Department Director Gerald H. Goldberg 1/29/97	Agency Secretary Date	By: Date:

State law provides a personal exemption credit of $67 for each taxpayer plus an additional personal exemption credit for each dependent and for those individuals who are over 65 years of age or are blind. The personal exemption credit is adjusted annually for inflation.

Since the sunset of the earlier low-income tax credit, California has not had a low-income tax credit of general application; however, there is a limited low-income credit for certain Enterprise Zone employees.

This bill would provide a nonrefundable low-income tax credit for all taxpayers equal to a percentage, determined by the taxpayer's state AGI, multiplied by the taxpayer's "net tax." "Net tax" is the total amount of tax imposed less the allowable personal exemption credits. This bill would provide that the low-income tax credit could only be taken after all other allowable, nonrefundable credits have been taken.

The applicable percentage amount would be determined as follows:

For single, married filing separate, or head of household taxpayers:

If the adjusted gross income is:	The percentage is:
$8,920 or less	100%
Over $8,920, but not over $10,160	80%
Over $10,160, but not over $11,360	60%
Over $11,360, but not over $12,570	40%
Over $12,570, but not over $13,790	20%
Over $13,790	0%

For married filing joint or surviving spouse taxpayers:

If the adjusted gross income is:	The percentage is:
$17,880 or less	100%
Over $17,880, but not over $20,490	80%
Over $20,490, but not over $22,710	60%
Over $22,710, but not over $25,100	40%
Over $25,100, but not over $27,550	20%
Over $27,550	0%

This bill would provide that the tax credit would not be allowed to:

- taxpayers who are required to pay the alternative minimum tax during the taxable year;
- trusts or estates subject to tax; or
- taxpayers who are nonresidents as of the close of the taxable year for which the credit is claimed.

This bill would provide for indexing the credit by recomputing AGI brackets to adjust for inflation.

Policy Considerations

This bill would not allow the credit to be available to nonresidents. This raises the question of constitutionality given its discriminatory nature.

Implementation Considerations

The implementation of this bill would require some changes to existing tax forms and instructions and information systems, which could be accomplished during the normal annual update. However, to make this credit more accessible to low-income taxpayers, the department would add this credit to the 540A and 540EZ, which do not currently allow credits other than exemption credits. These changes would require an additional line on some forms and additional pages in certain booklets for instructions, resulting in increased costs.

Taxpayer error would probably increase since taxpayers would not be able to rely solely on tax tables to determine the tax they owe. Rather, taxpayers, many of whom may be unsophisticated, would (1) determine their “net tax” from the applicable tax table, (2) individually arrive at the applicable percentage of allowable credit, and (3) reduce “net tax” by the allowable low-income credit to arrive at the tax they owe.

Technical Considerations

This bill uses AGI brackets to determine the applicable credit percentages for each taxable year beginning January 1, 1997. This bill also provides for the indexing of these brackets for each taxable year beginning on or after January 1, 1997. The attached amendment would change the year in which the brackets start being recomputed to 1998.

FISCAL IMPACT

Departmental Costs

This bill would have significant impact to certain systems in the department and the costs are estimated at $350,000 for the first year with ongoing costs of $230,000. In addition, this bill would result in additional costs of approximately $1.1 million for the printing and publishing of additional pages to the 540A/540EZ booklet.

Tax Revenue Estimate

Assuming enactment at the earliest by mid-year 1997, the revenue impact of this proposal is estimated as follows:

Adjusted Gross Income		**Taxable Year** (In Millions)			**Fiscal Year *** (In Millions)		
		1997	**1998**	**1999**	**1997/8**	**1998/9**	**1999/00**
$ -	$ 5,000	($5)	($5)	($5)	($7)	($5)	($5)
$ 5,000	$10,000	($9)	($9)	($9)	($13)	($9)	($10)
$10,000	$15,000	($11)	($12)	($12)	($16)	($12)	($12)
$15,000	$20,000	($1)	($1)	($1)	($1)	($1)	($1)
$20,000	$25,000	($4)	($4)	($4)	($6)	($4)	($4)
$25,000	$30,000	($3)	($3)	($3)	($4)	($3)	($3)
Total		($33)	($34)	($34)	($47)	($34)	($35)

* Assumes withholding tables would be revised to allow for the credit.

This estimate does not account for changes in employment, personal income, or gross state product that might result from this proposal.

Tax Revenue Discussion

The revenue impact of this proposal would depend on the number of individuals claiming the credit and the average credit claimed.

The above estimate was based on the department's income tax model and estimated to be claimed on approximately 1.2 million returns. The fiscal year estimates assume withholding tables would be revised to allow for the credit.

POSITION

Neutral.

The staff's position is determined by administrative considerations and does not take into account tax revenue impact on the state. However, such issues are discussed in the analysis.

Analyst	Paul Brainin
Telephone #	845-3380
Attorney	Doug Bramhall

FRANCHISE TAX BOARD'S
PROPOSED AMENDMENTS TO SB 83
As Introduced December 16, 1996

AMENDMENT 1

On page 6, line 2, strikeout "1997" and insert:

1998